

**State Budget Office  
Office of Financial Management  
Support Services Division  
Internal Audit Program**

**Contract Purchasing Cycle**

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**Audit Objective**

The purpose of this audit is to ensure compliance with established regulations, policies and procedures. Audit objectives are to review a sample of purchases for proper approval, appropriate accompanying documentation, reasonableness and proper accounting.

**Risk**

Related risk in this area is the possibility of entering a Purchase Requisition without a valid Blanket Purchase Order (BPO) number.

**Audit Program Standards**

This audit program is designed to document and obtain a sufficient understanding of relevant management controls that are in effect. Consideration should be given to any prior audit findings and whether corrective action has occurred. At the conclusion of fieldwork, all findings and recommendations for improvement should be documented.

**General Description**

Management and Budget Act 431 of 1984 prescribes powers and duties of the Department of Management and Budget (DMB). The Act authorizes the Department to issue directives and to provide for centralized administrative services such as purchasing. The Department shall provide for the purchase of, the contracting for, and providing of the supplies, materials, services, insurance, utilities, third party financing, equipment, printing and all other items as needed by State agencies for which the legislature has not otherwise expressly provided.

ADPICS transactions are assigned a commodity code based on the good or service requested. Some of these commodity codes reference BPOs. ADPICS does not require the BPO number to be entered for the transaction to be successfully processed.

**References**

- Policy 0610 entitled "Contracting"
- Procedures 0620.01 titled "Obtaining State Administrative Board Approval"
- Procedures 0620.02 titled "Submissions to the Finance and Claims Committee"
- Management and Budget Act, Public Act 431 of 1984 as amended, sub sections 261-264

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**Test Sample**

Develop a script in CLEAR ACCESS that will extract ADPICS initiated expenditure transactions for a given fiscal year and agency. The essential part of the criteria will look for "BP" document type and null in the BPO number field.

**Exclusions for Non DMB-Acquisition Services Procurements**

There are certain procurements that do not go through DMB-Acquisition Services. Verify the sample selection of purchases does not fall into one of these categories:

1. Special personal services paid via State payroll
2. CS-138 contracts for personal services
3. Grants
4. Procurements of services exempted by specific statutory authorization which supersedes Public Act 431 of 1984
5. The activities are handled by DMB-Office of Facilities and are services performed by non-State personnel relating to:
  - Building construction
  - Alteration, repair
  - Installation
  - Painting, decorating
  - Completion
  - Demolition
  - Conditioning, reconditioning
  - Improvements
  - Hazardous waste studies
  - Clean up, transport and disposal
6. Expert Witnesses (a Letter of Agreement must be signed)

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**Audit Program for Section.261:**

	YES	NO	N/A	COMMENTS	WP
Review and verify that OFM-DMB guidelines were properly established and are being adhered to for the following areas:					
a) Supplies					
b) Materials					
c) Services					
d) Insurance					
e) Utilities					
f) Third party financing					
g) Equipment					
h) Printing					
i) All other items					

**Michigan Based Firms**

Review and verify the selection process to determine that preference was given to products manufactured or services offered by Michigan-based firms, all other things being equal.					
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**Competitive Bids**

Review and verify that any competitive bids were solicited from the private sector (whenever practical) to efficiently and effectively meet the State's needs.					
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**Discretionary Decisions**

Review and verify that the department made all discretionary decisions concerning State contracts in the areas of:					
• Solicitation awards					
• Amendments					
• Cancellations					
• Appeals					

**Alternative Procurement Method**

Review and verify those procurement methods the department used which were in the best interest of the State that did not require competitive bidding pursuant to subsection (1).					
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**Delegated Authority**

	YES	NO	N/A	COMMENTS	WP
Confirm whether the department delegated its procurement authority to other State agencies.					
Confirm if a dollar limit was established and adhered to (for the delegation).					
Verify that the State agencies complied with departmental procurement directives.					

**Lease Purchases**

Review procedures and verify a sample of lease and installment purchases to determine they do not exceed the anticipated useful life of the item purchased, unless prohibited by law.					
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**Standards**

Select a test sample; verify directives issued by the department, standard specifications, and standards of performance are being adhered to (for the following):					
a) Procurement					
b) Receipt					
c) Inspection					
d) Storage of supplies					
e) Materials					
f) Equipment					
g) Printing					
h) Services					

**Cooperative Purchasing**

Verify established procedures used to ensure the department's directives on cooperative purchasing agreements are being complied with.					
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**Contract File**

	YES	NO	N/A	COMMENTS	WP
<p>Effective oversight by a contract Administrator will increase the probability that expectations associated with a project or service are fulfilled in a responsible fashion. Verify the agency maintains a contract file containing:</p> <ul style="list-style-type: none"> <li>Requests for Information (RFI), Proposal (RFP) or Quotation (RFQ)</li> <li>Contractor's responses</li> <li>Contract (formal contractual document or purchase order)</li> <li>Complaint to vendor</li> <li>Correspondence and memos</li> <li>Progress reports</li> <li>Contractor's invoices and supporting documentation</li> <li>Draft deliverables</li> <li>Final deliverables</li> <li>Post-project evaluation</li> </ul>					

**Vendor Performance**

<p>All contracts for commodities and services made through DMB-Acquisition Services are subject to continuing supervision of DMB-Acquisition Services. The contract Administrator or agency personnel should use the formal vendor performance process through ADPICS when problems with vendors cannot be resolved.</p> <ul style="list-style-type: none"> <li>• Verify the vendor was given adequate notice and an opportunity to improve performance or refute the complaint.</li> <li>• Verify that notification was given to the vendor close to the incident.</li> <li>• Verify the Vendor Performance notification document was created in ADPCS by utilizing screen 5260.</li> <li>• Determine that DMB-Acquisition Services made the determination of validity.</li> </ul> <p>Verify that the vendor was informed of specific areas of deficient performance. Note the measures that were necessary to confirm to contractual requirements.</p> <p>Determine if a date was given to the vendor to either comply or indicate reasons for failure and possible remedies.</p>					
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**Audit Program Conclusion**

Prepare a brief narrative summarizing audit findings and their implications to the department.  Prepare a brief narrative describing recommendations for improvement.  All audit review points have been discussed with the supervisor and incorporated into the final report.	<b>YES</b>	<b>NO</b>	<b>N/A</b>	<b>COMMENTS</b>	<b>WP</b>
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Reviewed By: _____	Date _____ —

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**Contracts for Personal Services (Rule 4-6.1)**

**Audit Objective**

The purpose of this audit is to ensure compliance with established regulations, policies and procedures. Audit objectives are to review a sample of Personal Service Contracts for proper approval, appropriate accompanying documentation, cost savings, reasonableness and proper accounting.

**Risk**

Personal service contracts authorized by Department of Civil Service may not be properly coded, authorized, or adhere to State guidelines.

**Audit Program Standards**

This audit program is designed to document and obtain a sufficient understanding of relevant management controls that are in effect. Consideration should be given to any prior audit findings and whether corrective action has occurred. At the conclusion of fieldwork, all findings and recommendations for improvement should be documented.

**General Description**

“Contracts for personal services” means a contract between a State agency and a contractor pursuant to which the State agency is obligated to make disbursements from appropriated funds for the personal services of persons who are not classified employees of the State. The personal services are uncommon to the State classified services because they are so specialized, technical, peculiar or unique in character that the talent, experience or expertise required to accomplish the duties and responsibilities cannot be recognized as normal to State service and cannot be efficiently included in the classification plan.

The Electronic CS-138 is used by agencies to Request to Contract for Personal Services as an approval system for the acquisition of services that are specifically authorized by Department of Civil Service. These types of services are uniquely coded in ADPICS to indicate their status. State policy is:

Unless excluded...all purchase agreements with independent contractors that are for commodities or services that provide a direct benefit to the State of Michigan...must be recorded into ADPICS...

**References**

- Michigan Constitution, 1963, Article 11, Section 5
- Reference Chapter 4, Classification Rule, Sections 4-6: Contracts for Personal Services
- Policy 0610 entitled “Contracting”
- Management and Budget Act, Public Act 431 of 1984 as amended, subsections 261-264
- Procedure 0620.02 - entitled “Submissions to the Finance and Claims Committee”

**Test Sample**

Develop a script in CLEAR ACCESS that will extract ADPICS initiated expenditure transactions for a given fiscal year and agency. Specifically look for dollar amounts over predetermined amount and commodity codes that fit the Department of Civil Service personal service criteria. Sample these records to ascertain compliance with data entry and coding controls.

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**Audit Testing**

	YES	NO	N/A	COMMENTS	WP
Verify the CS-138 form was authorized for purchases in excess of \$5,000 before the agency acquired any personal services from a person classified as a nonState employee. a) Civil Service must grant approvals before an appointed authority can make disbursements for personal services are obtained. b) Agencies can submit a Personal Service Contracts Request for approval under 1 or more of the 4 standards of Civil Service Rule 4-6.3.					

**CS-138 Cost Savings**

Personal Service Contracts should be performed at substantial savings to the State over the life of the contract when compared to the same level of service performed by the Classified Service. However, the projected savings over the life of the contract must also exceed the realized savings over the long term.  Savings are substantial if the contract for personal services results in average annual savings equal to or greater than the savings computed using the standard D minimum cost savings table, below.					
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**STANDARD D MINIMUM COST SAVINGS TABLE**

<b>Col 1 Average Annual Contract Cost:</b>		<b>Col 2 Average Annual Savings Must Equal</b>
From	To	
\$ -	\$ 5,000	None (Preauthorized)
\$ 5,001	\$ 25,000	25%
\$ 25,001	\$ 50,000	20% - Minimum \$6,250
\$ 50,001	\$ 100,000	15% - Minimum \$10,000
\$ 100,001	\$ 200,000	12.5% - Minimum \$15,000
\$ 200,001	\$ 500,000	10% - Minimum \$25,000
\$ 500,001	\$ 1,000,000	Minimum \$50,000
\$ 1,000,001	\$ -	5%

**Determining CS-138 Cost Savings**

	<b>YES</b>	<b>NO</b>	<b>N/A</b>	<b>COMMENTS</b>	<b>WP</b>
<p>Verify that estimated cost saving meets the “substantial savings” test. There are 4 key steps to this process.</p> <ol style="list-style-type: none"> <li>1. Compare estimated cost with the cost of providing those services through the State. Determine the average yearly cost of the proposed contract.</li> <li>2. Refer to the standard D minimum cost savings table to determine what the annual cost savings % should be.</li> <li>3. Using the figure in column 2, determine the minimum savings required for the proposed contract. If there is a percent stated, multiply that percentage by the average annual cost. For those categories reflecting a minimum amount the annual savings figure must exceed or meet those amounts.</li> <li>4. Compare the result from step 1) with the result from step 3). The proposed savings are substantial if step 1) is greater than step 3).</li> </ol>					

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**Audit Program Conclusion**

	YES	NO	N/A	COMMENTS	WP
Prepare a brief narrative summarizing audit findings and their implications to the department.					
Prepare a brief narrative describing recommendations for improvement.					
All audit review points have been discussed with the supervisor and incorporated into the final report.					

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**Audit Objective**

The purpose of this audit is to ensure compliance with established regulations, policies and procedures. Audit objectives are to review a sample of purchase orders for proper approval, appropriate accompanying documentation, reasonableness and proper accounting.

**Risk**

Inherent risks in this area are that unauthorized purchases may be made by unauthorized individuals, invalid items may be requisitioned, incorrect commodity codes may be used on Purchase Requisitions, Purchase Requisitions may be routed to both central and agency purchasing activities, ineligible vendors may be asked to bid, vendors may be selected on other than best price or value basis, a Purchase Order may be issued without standard legal terms, encumbrances may be charged to the wrong account or department, fictitious companies could be set up on the vendor file, and approvals may not occur timely.

**Audit Program Standards**

This audit program is designed to document and obtain a sufficient understanding of relevant management controls that are in effect. Consideration should be given to any prior audit findings and whether corrective action has occurred. At the conclusion of fieldwork, all findings and recommendations for improvement should be documented.

**General Description**

Executive Branch Departments and Sub-units shall acquire supplies, materials, services, insurance, utilities, third party financing, equipment, printing, or any other item for which the legislature has otherwise expressly provided, in compliance with applicable statutory and regulatory requirements concerning procurement.

**References**

- Procedure 0510.2 entitled "Procuring commodities – general"
- Management and Budget Act, Public Act 431 of 1984 as amended, sub sections 261-264

**Test Sample**

Obtain a test sample of purchase order documents from DMB-Support Services Division. The initiated expenditure transactions can be extracted from ADPICS by using script ADP97AE2.CLS. The script will produce a file that is downloadable to Microsoft ACCESS. When performing the download, ascertain that all fields are appropriately delimited and defined. Write an ACCESS Query using the following criteria:

DOC Type equal to DT  
Voucher Type equal to V

The extracted query file may be exported as a tab format file to software capable of performing statistical analysis and sampling (AuditForce used ACL for this purpose). To select a sample perform the following:

- Stratify the query file into high, medium, and low dollar strata
- Select a sample from the high dollar strata
- Select a sample from medium and low dollar strata by applying random sampling techniques
- Reformat statistical samples to Microsoft EXCEL to produce sample listings
- Forward the sample listing to selected agencies for document retrieval

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**Purchase Orders**

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**Office of Purchasing**

	YES	NO	N/A	COMMENTS	WP
Determine that DMB-Acquisition Services received the requisition from the agency and matched it with attachments.					
Verify commodity code number is correct.					
Verify receipt of necessary approvals.					
Verify the requisition was complete and clear.					
Verify the commodity or service requested was not a set-aside issue.					
Verify the request did not require a justification letter.					
Ensure aware criteria were proper in selecting the vendor.					
Determine that DMB-Acquisition Services has proper procedures to ensure desired substantive changes or requests for additional information are processed within a reasonable time frame.					
Determine that DMB-Acquisition Services held a pre-bid meeting.					

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**Purchase Orders**

**General Controls**

	YES	NO	N/A	COMMENTS	WP
<p>Determine the purchase of commodities was requisitioned through DMB-Acquisition Services unless they meet one or more of the following criteria:</p> <ul style="list-style-type: none"> <li>a) Under \$1,000 (some departments are at \$2,500) then a Procurement card is to be used</li> <li>b) Not on a Blanket Purchase Order (BPO)</li> <li>c) Designated as a Grant</li> <li>d) Office supplies BPO</li> <li>e) Exempted by specific statutory authorization which supersedes Public Act 431 of 1984, as amended</li> <li>f) Purchasing authority delegated to procurement staff of the department</li> <li>g) When non-State personnel are engaged the following activities are handled by DMB-Office of Facilities- <ul style="list-style-type: none"> <li>Building construction</li> <li>Alterations</li> <li>Repairs</li> <li>Installation</li> <li>Painting</li> <li>Decorating</li> <li>Completion</li> <li>Demolition</li> <li>Conditioning, reconditioning</li> </ul> </li> <li>a) Emergency Purchases</li> <li>b) Commodities from Sheltered Workshops</li> <li>c) Equipment Rentals</li> <li>d) Sole Source for Repairs or Replacement Parts</li> <li>e) Sole Source for Copyright Materials</li> <li>f) Printing <ul style="list-style-type: none"> <li>1. Rapid copy orders from DMB, Office Services Copy Center on Rapid Copy Order form (DMB-551) or Quick Copy Service Request Forms (DMB/OSD-503)</li> <li>2. DMB Print and Graphic Services Non-Contact Printing must be requisitioned through DMB-Acquisition Services</li> </ul> </li> </ul> <p>Determine the correct forms were used, where required in the test sample:</p> <ul style="list-style-type: none"> <li>Notice of Contract Agreement/Change Notice to Contract Agreement (DMB-234A)</li> <li>Invitation to Bid (DMB-285)</li> <li>Advice of Change (DMB-286)</li> <li>Purchase Order (DMB-287)</li> </ul>					

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	YES	NO	N/A	COMMENTS	WP
<p>Determine if the commodity is available from existing State BPO, Michigan State Industries (MSI), or on set-aside. If yes, ensure a contract release/direct purchase order (DPO) or BPO was issued.</p> <p>Ensure justifications were written for exemptions to an existing State BPO.</p> <p>Ensure justifications were written for exemptions relating to a single source.</p> <p>Determine that all delivery schedules or service periods are clearly identified.</p>					

**Audit Program Conclusion**

<p>Prepare a brief narrative summarizing audit findings and their implications to the department.</p> <p>Prepare a brief narrative describing recommendations for improvement.</p> <p>All audit review points have been discussed with the supervisor and incorporated into the final report.</p>					
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**Control Points**

**1.1 Purchase Request**

	YES	NO	N/A	COMMENTS	WP
Verify that all requisitions are reviewed and approved at the appropriate level prior to creation of the Purchase Order.					

**1.2 Set Up Requisition on ADPICS**

Verify all purchases are applied to an open appropriation.					
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**1.3 ADPICS Determines Approval Level Required**

Determine that proper approval path was adhered to based on commodity code and estimated dollar amounts from the purchase requisition. NOTE: Most personal service contracts require approval from Civil Service.					
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**1.4 Requisition Sent to Appropriate Approver's Mailbox**

Verify that all purchases are applied to an open appropriation, i.e. valid 20/D23 combination.					
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**1.5 Agency and Central Purchasing**

Determine that the agency had proper purchasing authority based on dollar level (generally up to \$1,000) and commodity type.					
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**1.6 Competitive Bid Process**

Verify the vendor only sends technical and price proposals to the department involved (when the purchase is within their delegated authority). For all other purchases, they should send the technical and price proposals back to DMB-Acquisition Services.					
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**1.7 Quick Purchase Program**

Determine that the Quick Purchase was between \$1,000 and \$25,000 (see Quick Purchase audit section).					
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**1.8 Award Determination**

	YES	NO	N/A	COMMENTS	WP
Verify the required documentation was on file prior to the contact being awarded.					

**1.9 Purchase Order Set Up on ADPICS, Encumbrance Recognized**

Verify that encumbrances are recorded (when PO's are posted and contracts are signed), and as such represent legal obligations to purchase goods or services.					
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**Audit Program Conclusion**

Prepare a brief narrative summarizing audit findings and their implications to the department.					
Prepare a brief narrative describing recommendations for improvement.					
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